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THE CONFERENCE BOARD

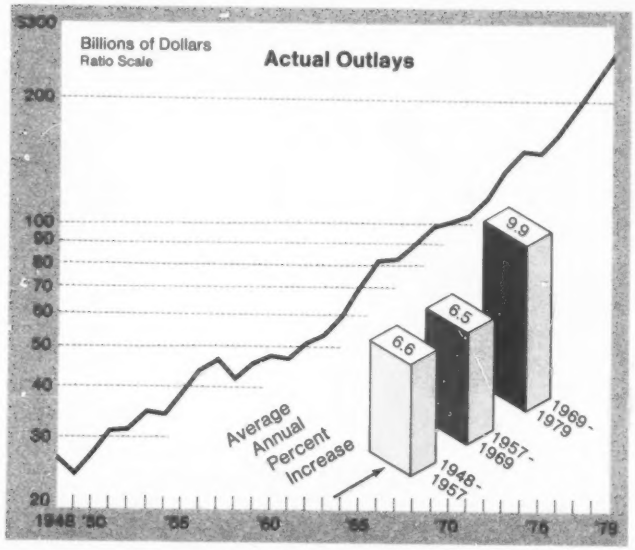
Capital Investment in Perspective

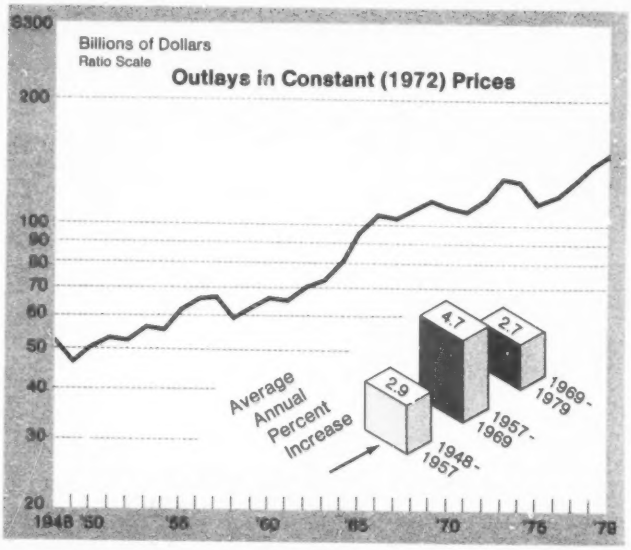
Economic Road Maps
Nos. 1886 - 1887

September, 1980

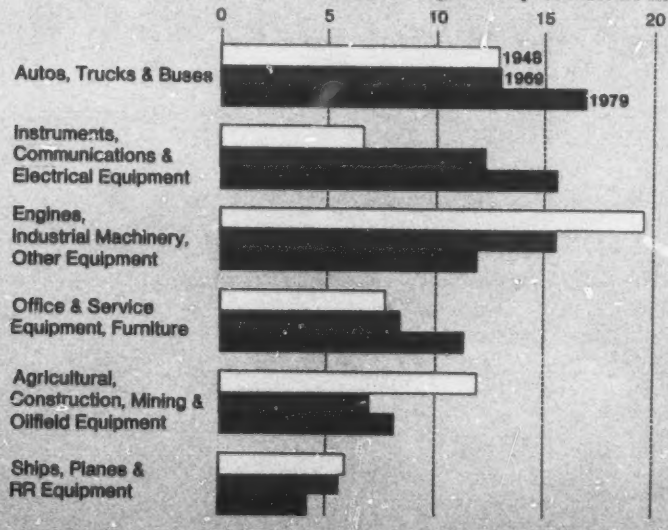
Most of the output of the U.S. economy is used up, or "consumed," not long after it is produced. That part of the national output that is not consumed consists of investment goods—structures and equipment that will be employed in the production process over a period of years and thus be used up only gradually. The amount of investment that our economy makes in equipment and structures today is a key determinant of our ability to produce a rising total volume of goods and services in the future, and to keep a growing labor force productively employed. Capital investment increased very rapidly in the 1960's, then shifted to slower growth in the past decade. Proposals to stimulate capital investment are being widely discussed this year, with particular emphasis on tax measures aimed at making investment more attractive financially.

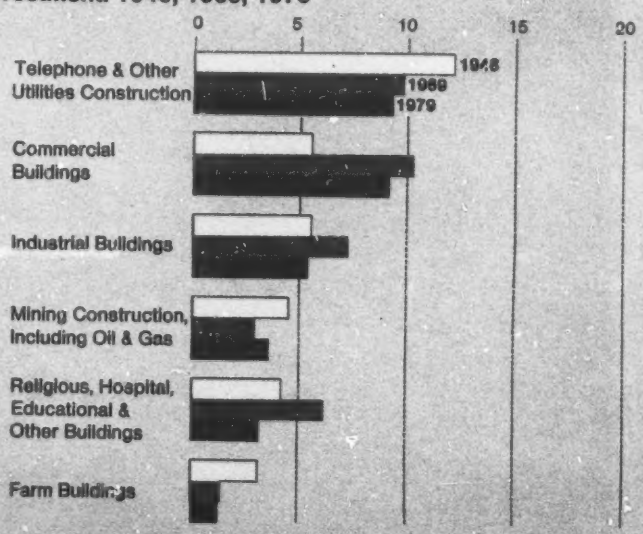
Private, Nonresidential Fixed Investment

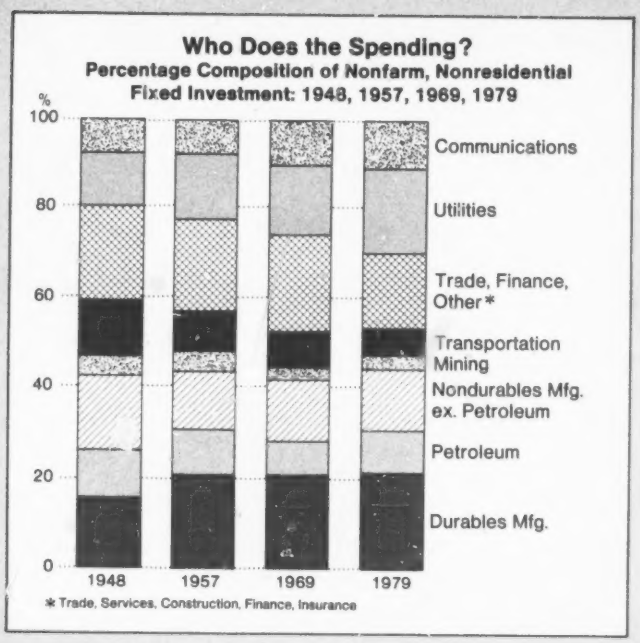




Percentage Composition of Investment: 1948, 1969, 1979

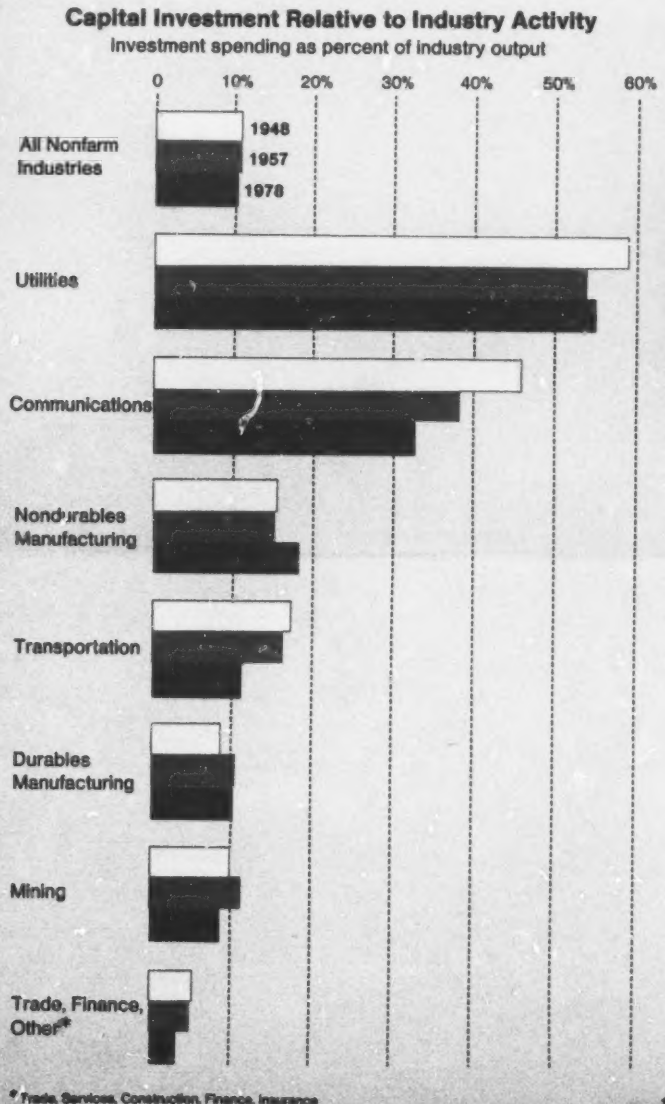


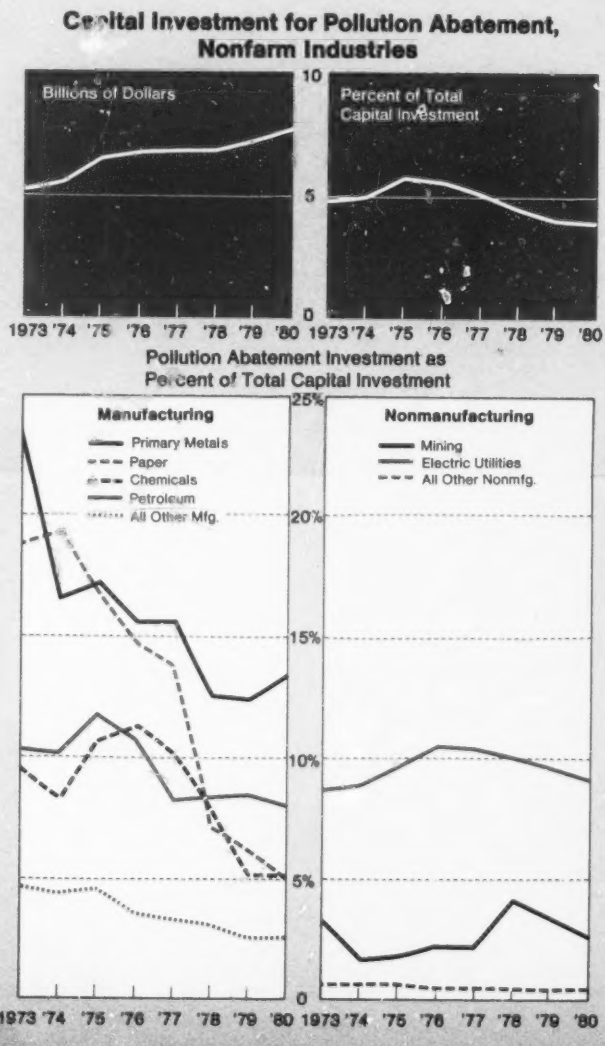


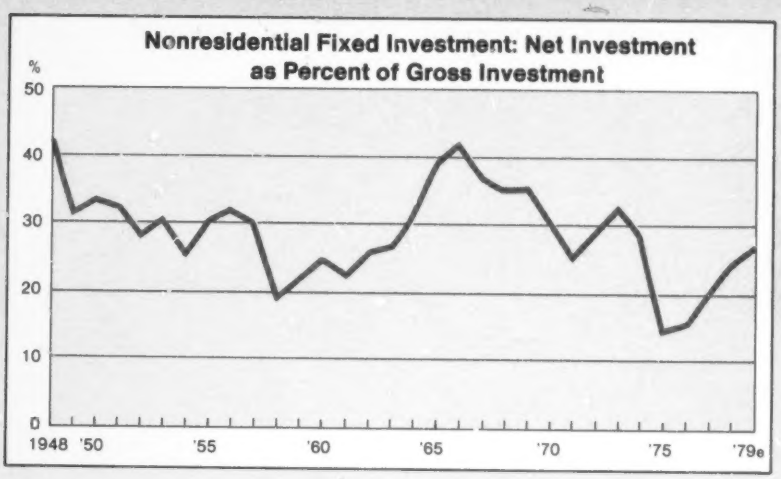


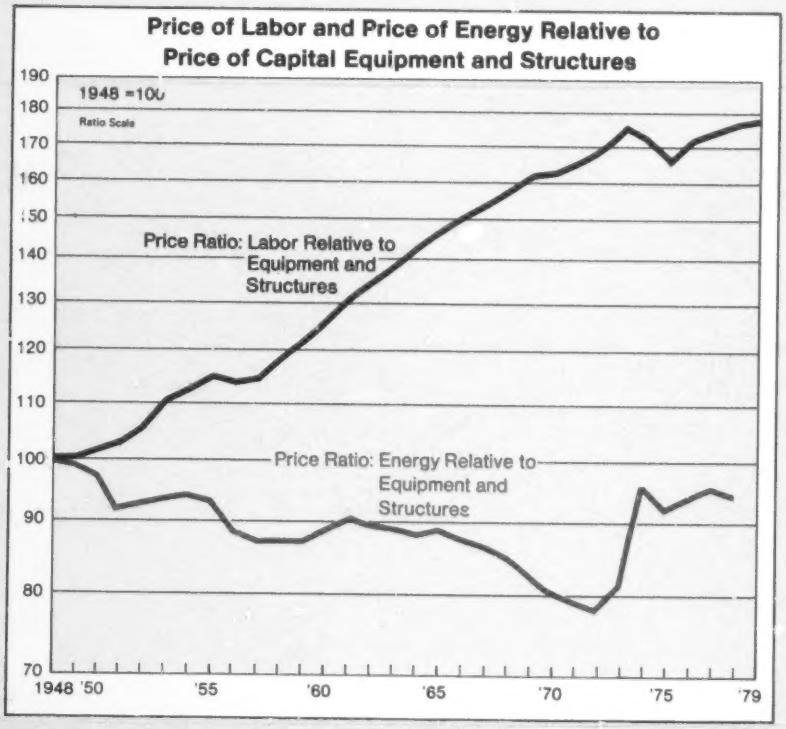
Private investment in equipment and nonresidential structures totaled $255 billion last year. (New housing, on which outlays last year were $114 billion, is also investment but is not considered here.) Autos, trucks and buses are currently the largest single major category of investment, comprising 17% of outlays in 1979 (lower chart on page 1). Industrial machinery accounted for only 12% of total outlays last year; 20 years ago, this category was 20% of total spending.

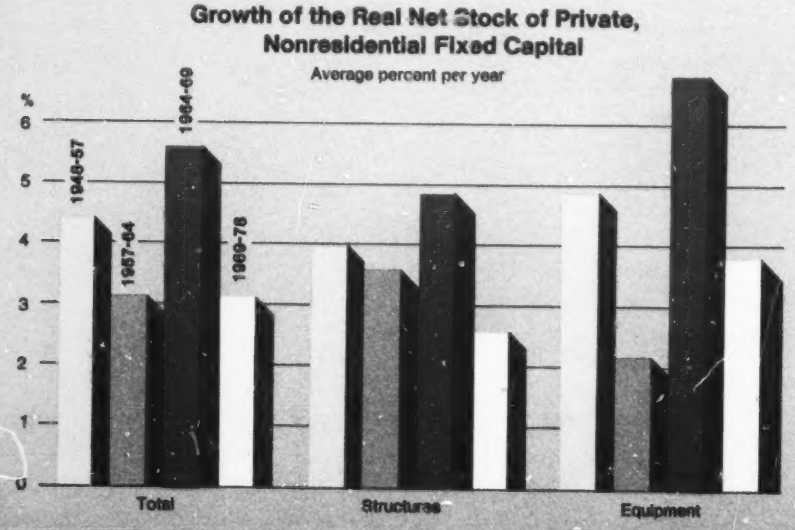
Durable goods manufacturing is the biggest capital spender among the major industries. Last year, durables manufacturers accounted for 21.5% of nonfarm, nonresidential investment spending; the utilities were next, with 18.5 percent. (See chart at left. The years used in that chart, and in the calculation of averages and growth trends, are peak years of the business cycle. This choice of years minimizes cyclical fluctuations in the data.) Although the utilities rank only second in share of total capital outlays, they are far in the lead when their capital spending is compared to their overall activity. The lower left panel shows that in 1978 (the last year for which suitable data are available), the











Average Ratio of Net Investment to Gross Investment

Percent

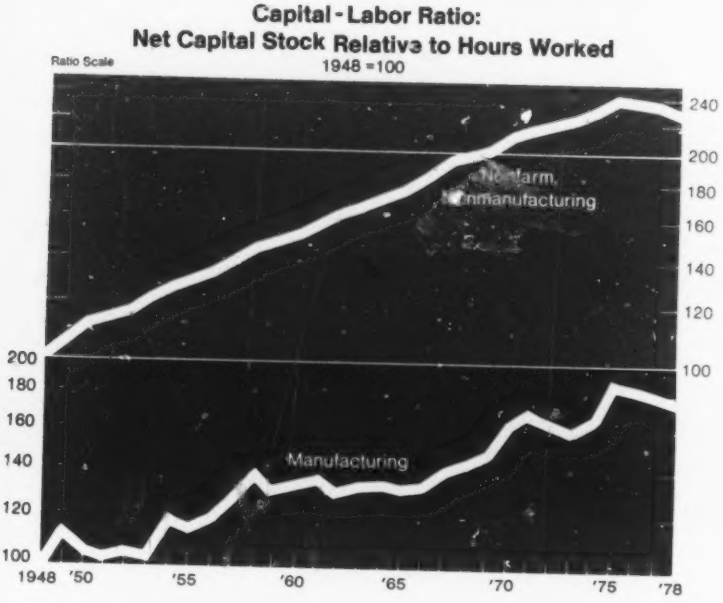
	1948-1957	1958-1964	1965-1969	1970-1979
Total	31.6	24.6	37.7	24.9
Structures	37.6	38.9	46.7	32.0
Equipment	27.1	13.7	31.9	20.9

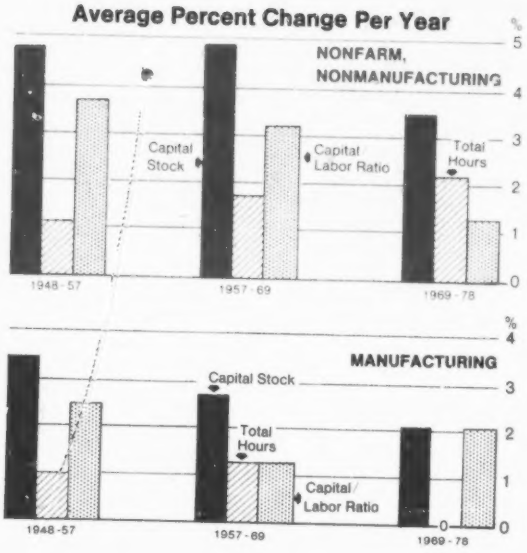
utilities' capital investments were equal to 55% of the value of the industry's output. The figure was 32% for the communications industry, in which telephone companies are a major element, but considerably lower in less capital-intensive industries. (An industry's output is measured here as its "value added," that is, the difference between its sales and its purchases from other industries. This is its contribution to GNP.)

Not all capital outlays are for equipment and structures to be used directly in the production of conventional goods and services. An important element in total capital spending, certainly during the past decade, has been spending for pollution abatement. In this case, the capital goods are used in production of cleaner air and water. In 1980, capital spending for pollution abatement is projected to be almost 4% of total nonfarm, nonresidential capital spending (lower right, page 2). Not surprisingly, the pollution abatement share of spending is highest in the metals, paper, chemical and petroleum industries. Outside manufacturing, it is very small except in the electric utility and mining industries.

The capital spending data on pages 1 and 2 are "gross." This means that they include expenditures to replace facilities that are ending their useful lives as well as for net additions to the capital stock. It is generally easier to estimate total capital spending than to estimate just that portion which is for net additions to the capital stock, but some data on net investment are available. Last year, net investment was only about 27% of gross investment (top chart, this page).

Reflecting the lower ratio of net to gross investment in the 1970's, the growth of the nation's capital stock has slowed from an average 5.6% per year



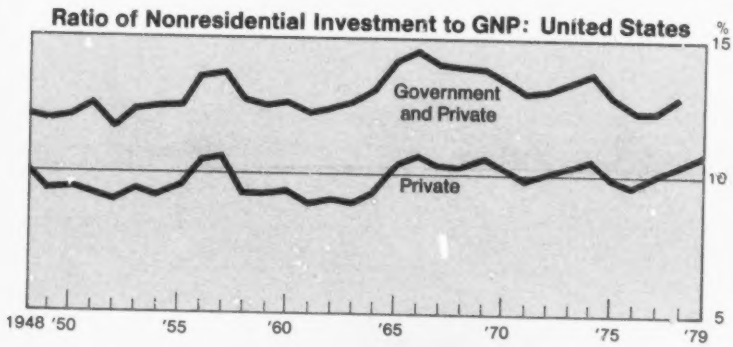


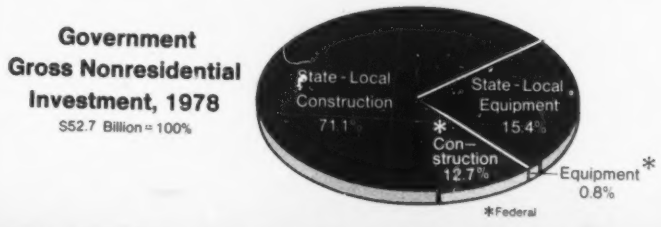
between 1964 and 1969 to an average 3.1% between 1969 and 1978 (lower chart on page 3). These are growth rates of the real net capital stock; this is the value, in constant prices, of the capital stock after deducting the value of that part that has already been used up. Slower growth of the capital stock has translated into outright shrinkage, in recent years, in the capital/labor ratio (chart above).

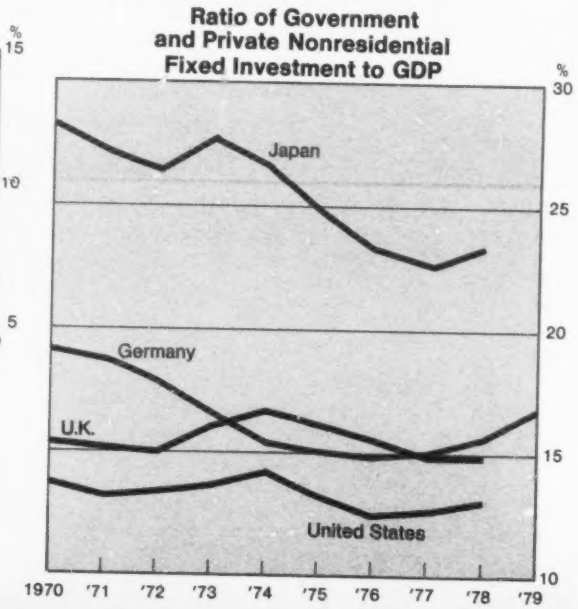
Other countries invest larger shares of their national output than we do. The chart at lower right shows capital investment as a share of national output in Japan (23% in 1978), Germany, (16%), the United Kingdom (15%) and the United States (13%). For this international comparison, it is necessary to include government investment. In the United States, this consists mostly of state and local government construction. Total government spending on fixed capital is under 3% of our GNP, as the chart at lower left shows. It also shows that, smoothing out the business cycle, we have been investing a very stable 10% to 11% of our GNP for many, many years.

Lora S. Collins

Sources: U.S. Department of Commerce, Bureau of Economic Analysis; The Conference Board.







ECONOMIC ROAD MAPS

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